

MEMORANDUM

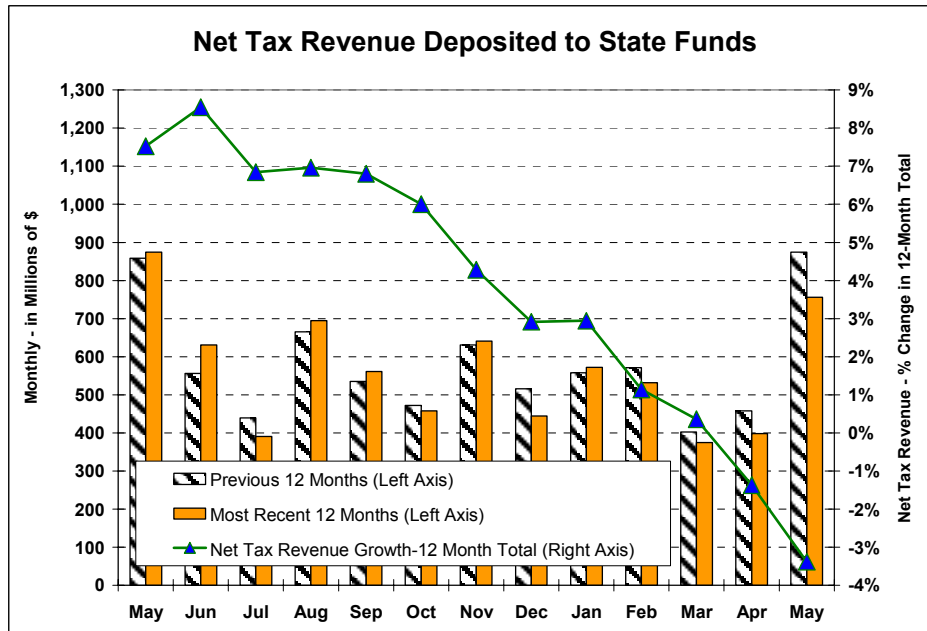
TO: Members of the Iowa Senate and
Members of the Iowa House of Representatives

FROM: Jeff Robinson
Shawn Snyder

DATE: June 16, 2009

Twelve-month Total Net Tax Receipts Through May 31, 2009

The attached spreadsheet presents net State tax revenue deposited to State funds for the 12-month period ending May 2009 with comparisons to the previous 12 months. May 2008 to May 2009 one-month comparisons are also presented. The source of the information is the State accounting system, including non-General Fund accounts. All accounting transactions related to taxes remitted to the State were reviewed, along with the refunds issued against those taxes.



Month of May Comparison

May net tax receipts totaled \$755.8 million, a decrease of \$118.4 million (- 13.5%) compared to May 2008. Major taxes and their contribution to the month's change include:

- Individual Income Tax (negative \$61.8 million, - 14.9%) – Gross income tax receipts decreased \$50.6 million in May as modest growth in withholding payments was eclipsed by significant declines in income tax payments with tax returns and quarterly estimate payments. Income tax refunds were \$11.2 million higher for the month. Monthly year-over-year negative net income tax growth is rare, with only ten instances over the past 48 months. Six of those instances occurred over the past eight months.
- Corporate Income Tax (negative \$10.5 million, - 19.8%) – Gross receipts decreased \$9.8 million and refunds increased \$0.7 million.
- Sales/Use Tax (negative \$37.9 million, - 13.0%)
 - Road Use Tax Fund use tax and fees for new registrations decreased \$5.7 million.
 - General Fund sales/use tax receipts increased \$2.5 million and refunds issued for the month increased \$34.7 million (net decrease of \$32.2 million). The large increases in gross receipts and in refunds are related to the recently-enacted statewide sales/use tax increase for school infrastructure coupled with the elimination of the local option sales tax for school infrastructure. This change boosts State sales/use tax receipts while increasing tax refunds by a similar amount, as the school infrastructure revenue is being removed from the State General Fund through a refund appropriation. This large decrease in General Fund sales/use tax receipts for the month of May offsets a large increase experienced in April, indicating a change in the timing of deposits.
- Fuel Tax (negative \$0.7 million, - 2.2%) – Gross fuel tax revenue decreased \$2.2 million while refunds processed in the month decreased \$1.5 million.
- Cigarette & Tobacco Taxes (negative \$1.8 million, - 8.5%) – The cigarette tax was increased from \$0.36 per pack to \$1.36 per pack on March 16, 2007. In addition, Iowa banned smoking in most public indoor locations effective July 1, 2008. Monthly cigarette and tobacco tax deposits have decreased at least 6.4% in each of the past five months, suggesting that the smoking ban may have had more of an impact on cigarette sales during the winter months. A \$0.62 per pack federal tax increase, effective April 1, 2009, will increase downward pressure on sales.
- Gambling Taxes (negative \$6.4 million, - 21.2%) – Gambling tax revenue is deposited weekly and May 2009 had four deposit days while May 2008 had five. This reverses a positive calendar impact experienced in April.

Year-over-Year Comparison – Net Tax Revenue

During the 12-month period ending May 2009, net revenue from all taxes deposited to State funds totaled \$6.453 billion, a decrease of \$226.0 million (- 3.4%) compared to the prior 12 months. Major contributors to the year-over-year dollar and percentage changes include:

- Individual Income Tax (negative \$96.6 million, - 3.4%) – The rate of individual income tax receipt growth has decreased significantly since peaking in May 2008 at 11.8% year-over-year. The processing of tax year 2008 returns over the past two months accelerated the decrease.
- Corporate Tax (negative \$81.8 million, - 23.2%) – In November 2008, annual net corporate tax receipt growth became negative for the first time since August 2004.

- Sales/Use Tax (negative \$23.9 million, - 1.1%) – Net sales/use tax receipts have been down five of the past six months compared to the same month the previous year and the annual percent growth has fallen from positive 4.1% to negative 1.1% over that time.
- Fuel Tax (negative \$9.1 million, - 2.0%) – Net motor fuel tax revenue has been weak the past twelve months, likely the result of higher fuel prices through July 2008 and declining economic activity since then. According to Department of Revenue taxable gallons sales reports, over the most recent 12-month period Iowa gasoline/ethanol gallons sold decreased 1.6% while diesel sales were down 6.3%, the seventh consecutive month showing a decline in annual diesel taxable sales.
- Gambling Tax (negative \$1.9 million, - 0.6%) – Despite a new Waterloo casino and expansion of the casinos in Clinton and Dubuque, three changes providing boosts to year-over-year gambling growth, gambling tax revenue is now modestly negative year-over-year. According to Racing and Gaming Commission statistics, eleven of Iowa's seventeen casino/track locations reported negative annual adjusted gross revenue (AGR) growth for the 12-month period ending May 2009. The AGR growth for all facilities was 0.01% over the past 12 months. Excluding the three new or expanded facilities, growth was negative 3.3%.
- Cigarette and Tobacco Tax (negative \$10.4 million, - 4.1%) – The second anniversary of the tax increase has passed and the tax increase no longer impacts the year-over-year growth calculation.
- Insurance Premium Tax (negative \$11.7 million, - 10.5%) – The insurance premium tax rate was reduced over multiple years and is now fully implemented. The lack of growth in insurance premium tax revenue may be the result of expanded use of tax credits, including credits earned through an insurance company's own activities as well as credits purchased from others.

Tax Spotlight – Franchise (Bank) Tax and Credit Union Tax

The taxation of banks and financial institutions in Iowa dates back to at least the 1851 Code of Iowa. Prior to HF 1294 (Taxation of Financial Institutions Act of 1970), the bank tax was essentially a property tax, collected and retained at the local level.

The current franchise tax (Chapter 422, Division V, Code of Iowa) is imposed on the net income of state banks, national banking associations, trust companies, federal and state chartered savings and loan associations, financial institutions chartered by the Federal Home Loan Bank Board, and production credit associations at a rate of 5.0%. An alternative minimum tax may be applicable to financial institutions at an effective rate of 3.0%. Credit unions are subject to a different tax discussed below.

The Iowa franchise tax enacted in 1970 provided for rates ranging from 5.0% to 8.0% of net income. The franchise tax rate was reduced to a flat 5.0% in 1980. Prior to 1995, financial institutions could transfer income-producing assets to non-bank subsidiaries reducing the franchise tax owed. Legislation was enacted beginning with tax year 1995 that prohibits the deduction of those types of transfers.

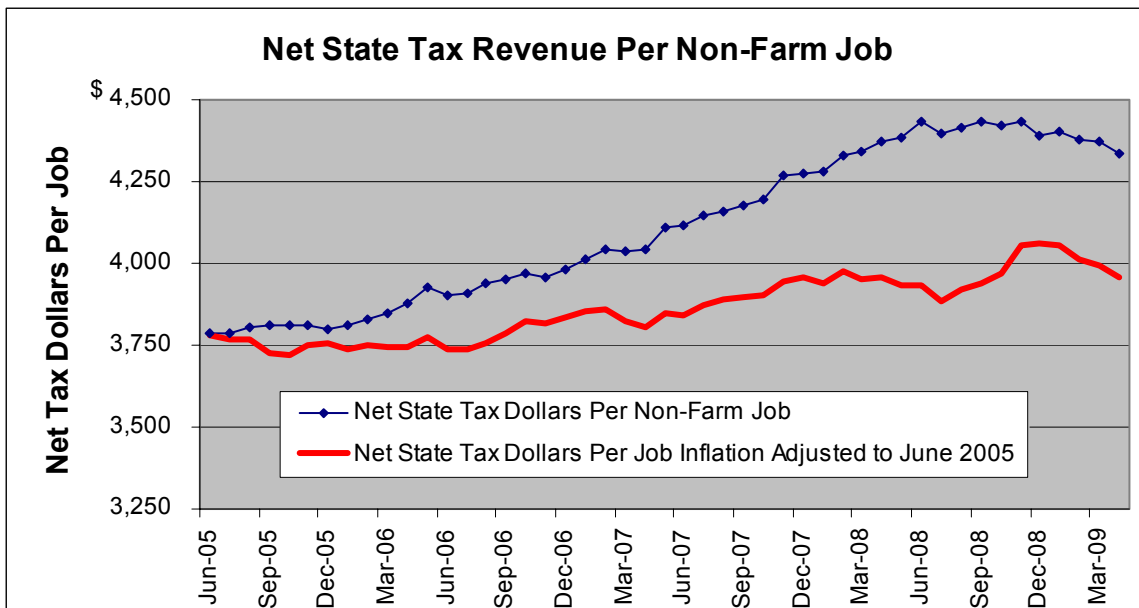
Tax returns for franchise tax are required to be filed by the last day of the fourth month after the end of the tax year. Estimate payments from most financial institutions are due on a quarterly basis. Revenue received from the franchise tax is deposited in the State General Fund. Section 15F.204(8b), Code of Iowa, appropriates \$7.0 million of franchise tax receipts annually to the Community Attraction and Tourism Fund through FY 2013. The appropriation occurs

after the money is deposited to the State General Fund so the franchise tax allocation is essentially a General Fund appropriation.

Credit Unions are taxed at a rate of five mills (0.5%) of “legal and special reserves” (see Section 533.329, Code of Iowa). The tax is imposed by the Board of Supervisors and the revenue from the tax is divided between the county, city, and State, with the State share equal to 50.0% of revenue collected. The State revenue is deposited to the General Fund.

Tax Revenue and Employment

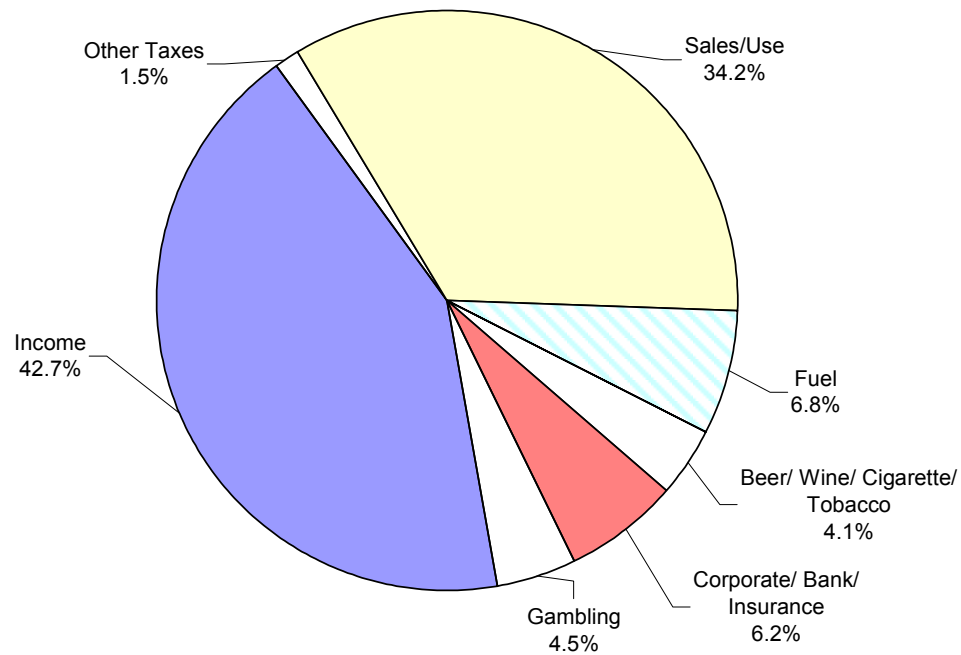
The average reading for Iowa non-farm employment over the 12 months ending April 2009 is 1,514,600, and net State tax receipts over the same 12 months totaled \$6.571 billion, or \$4,338 per non-farm job. This is \$553 (14.6%) higher than the per-job average for June 2005. Over that same time period, inflation (CPI-U) increased 9.6%. Therefore, tax revenue per job has exceeded the rate of inflation since June 2005 by roughly 1.3% per year. The following chart provides an historical perspective of tax collections per non-farm job and inflation-adjusted collections per job.



Net State Tax Revenue - Twelve Months Ending May 2009

Net Revenue = \$6.452 Billion

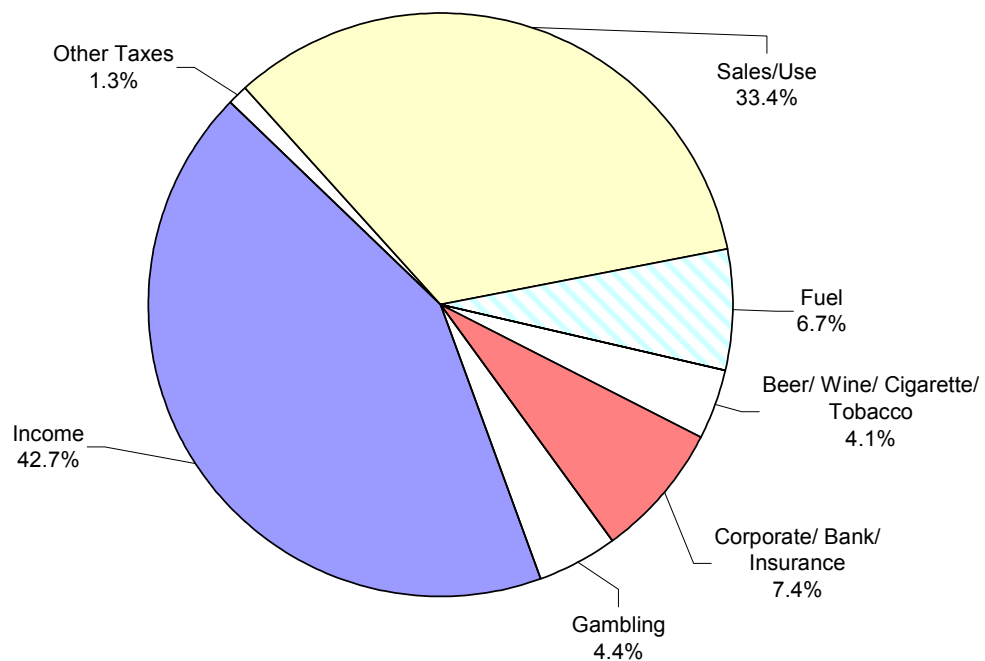
Percentages may not add to 100% due to rounding



Net State Tax Revenue - Twelve Months Ending May 2008

Net Revenue = \$6.678 Billion

Percentages may not add to 100% due to rounding



Net Tax Revenue Deposited to State Funds - Cash Basis

Dollars in millions - Columns and Rows may not add due to rounding

Net Tax by Tax Type	Previous 12-Month Period Total	Most Recent 12-Month Period Total	12-Month \$ Change	12-Month % Change	Month of May 2008	Month of May 2009	May \$ Change	May % Change
Banking	\$ 32.6	\$ 30.1	\$ - 2.5	-7.7%	\$ 3.6	\$ 3.1	\$ - 0.5	-13.9%
Beer & Wine	20.7	21.0	0.3	1.4%	1.7	1.7	0.0	0.0%
Cigarette & Tobacco	252.0	241.6	- 10.4	-4.1%	21.3	19.5	- 1.8	-8.5%
Corporate Income	352.5	270.7	- 81.8	-23.2%	52.9	42.4	- 10.5	-19.8%
Fuel	446.4	437.3	- 9.1	-2.0%	32.2	31.5	- 0.7	-2.2%
Gambling	295.5	293.6	- 1.9	-0.6%	30.2	23.8	- 6.4	-21.2%
Individual Income	2,850.7	2,754.1	- 96.6	-3.4%	415.7	353.9	- 61.8	-14.9%
Inheritance	74.5	75.5	1.0	1.3%	7.5	7.5	0.0	0.0%
Insurance	111.6	99.9	- 11.7	-10.5%	17.2	16.9	- 0.3	-1.7%
Other Taxes	- 4.5	8.8	13.3	--	- 1.4	- 0.1	1.3	--
Real Estate Transfer	17.8	15.1	- 2.7	-15.2%	1.1	1.3	0.2	18.2%
Sales/Use	2,228.7	2,204.8	- 23.9	-1.1%	292.2	254.3	- 37.9	-13.0%
Total Net Taxes	\$ 6,678.5	\$ 6,452.5	\$ - 226.0	-3.4%	\$ 874.2	\$ 755.8	\$ - 118.4	-13.5%
Gross Tax & Refunds								
Gross Tax	\$ 7,389.6	\$ 7,641.6	\$ 252.0	3.4%	\$ 931.9	\$ 857.5	\$ - 74.4	-8.0%
Tax Refunds	\$ - 711.1	\$ - 1,189.2	\$ - 478.1	67.2%	\$ - 57.6	\$ - 101.6	\$ - 44.0	76.4%
Net Tax Receipts by Fund								
State General Fund (GF)	\$ 5,705.4	\$ 5,498.7	\$ - 206.7	-3.6%	\$ 784.1	\$ 678.4	\$ - 105.7	-13.5%
Road Use Tax Fund	\$ 708.9	\$ 702.7	\$ - 6.2	-0.9%	\$ 59.6	\$ 53.1	\$ - 6.5	-10.9%
Non-GF Gambling	\$ 233.9	\$ 231.7	\$ - 2.2	-0.9%	\$ 30.0	\$ 23.5	\$ - 6.5	-21.7%
Other State Funds	\$ 30.3	\$ 19.3	\$ - 11.0	-36.3%	\$ 0.6	\$ 0.8	\$ 0.2	33.3%
Local Option Taxes *	\$ 713.1	\$ 784.7	\$ 71.6	10.0%	\$ 64.9	\$ 65.7	\$ 0.8	1.2%

* Sales, income, and hotel/motel. Distributed to local governments - not included in numbers above.

Numbers are rounded to the nearest \$0.1 million. Percentages are calculated after rounding.

Tax Categories Used in Table

Franchise (Bank) Tax: Taxes on banks are deposited to the State General Fund. State credit union tax is included on this line also.

Beer & Liquor Tax: Taxes on beer, liquor, and wine are deposited to the State General Fund, the Liquor Control Fund, and a small amount is deposited to a Department of Economic Development fund for wine promotion.

Cigarette & Tobacco Tax: Cigarette and the tobacco products tax revenue is deposited to the State General Fund.

Corporate Income Tax: All corporate tax is deposited to the State General Fund.

Motor Vehicle Fuel Tax: All motor vehicle fuel tax is deposited to one of two road use funds, with the exception of tax revenue from the sale of aviation and marine fuels.

Gambling Tax: The first \$60.0 million of gambling tax revenue each fiscal year is deposited to the State General Fund. Other funds receiving deposits of gambling tax revenue over the last 24 months include the School Infrastructure Fund, the Rebuild Iowa Infrastructure Fund, The Gambler's Assistance Fund, the County Endowment Fund, the Endowment for Iowa's Health Account, and the Vision Iowa Fund.

Individual Income Tax: Most individual income tax revenue is deposited to the State General Fund. Other destinations include the Workforce Development Fund (\$4.0 million) and Child Daycare Fund (\$2.6 million). In addition, several economic development programs are financed by individual income tax withholding. In those instances, the employer does not remit the tax withheld from employees and it is never deposited to a State fund. That revenue is not included here.

Inheritance Tax: All inheritance tax is deposited to the State General Fund.

Insurance Premium Tax: All insurance premium tax is deposited to the State General Fund.

Other Taxes: Other taxes include brucellosis eradication property tax (deposited to a Department of Agriculture and Land Stewardship fund), drug stamp tax (State General Fund), utility replacement property tax (State General Fund), and car rental tax (Road Use Tax Fund). Other taxes also include a suspense account used to hold tax deposits prior to determining the correct tax type for the money and tax revenue transferred by the Department of Revenue to separate accounts to fund tax collection activities (tax gap and Department operations).

Real Estate Transfer Tax: Real estate transfer tax is collected by counties. Counties retain 17.25% and remit the remainder to the State. The State deposits 95.0% to the State General Fund and 5.0% to the Shelter Assistance Fund. The distribution of real estate transfer tax revenue changes beginning FY 2010, when the State General Fund percentage begins a decline to 65.0% by FY 2015.

Sales/Use Tax: General sales/use tax is deposited to the State General Fund, while most vehicle use tax is deposited to the Road Use Tax Fund. Beginning FY 2009, the vehicle use tax was converted to a fee structure. To allow continuity of data, revenue from the fee structure is reflected in this document as tax revenue. Also beginning FY 2009, the School Infrastructure Local Option (SILO) sales tax was converted to a statewide 1.0% sales/use tax and the revenue from that statewide tax is transferred out of the State General Fund monthly through a refund appropriation. To allow for continuity of data, the refund transfers are subtracted as part of the net sales/use tax calculation.

Local Option Taxes: Local option taxes are presented at the bottom of the table and are not included in the numbers above. Prior to FY 2009, local option taxes included the SILO tax, Local Option Sales Tax (LOST) for local government finance, Local Option Income Surcharge for schools, and hotel/motel tax. Starting FY 2009, the SILO tax was converted to a 1.0% statewide tax and the SILO was eliminated. To allow for continuity of data, the transfers from the State General Fund as a result of the 1.0% statewide tax are included in the local option tax amount.

Report Database

The database for this report is the State accounting system. If transactions are incorrectly coded in the system as tax revenue or tax refunds, the numbers presented here will be impacted.